REAL ESTATE

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OUTLOOK

June 1989

A Monthly Forecast for the Economy and Real Estate

FORECAST SUMMARY

- The U.S. Department of Commerce cut its estimate of first quarter real GNP growth dramatically to 4.3 percent from 5.5 percent, indicating a much slower rate of economic activity in the opening months of 1989.
- The dollar reached a 29 month high in May, encouraged primarily by high U.S. interest rates relative to those in Germany, Japan and the U.K. In addition, political problems in Europe and Japan, higher oil prices, and the attraction of the U.S. stock and bond markets to foreign investors, all added to the new found interest in the dollar.
- In response to the recent rally in the bond market, which forced long-term rates down by over 50 basis points, fixed-rate mortgages have fallen to their lowest levels so far in 1989. The average rate on a conventional fixed-rate mortgage has plunged by almost 100 basis points in the past two months, to 10.5 percent in the final week of May.
- Prompted by a large drop in the construction of buildings with five or more housing units, housing starts slowed by 2.7 percent in April to an annual rate of 1.361 million units. However, starts of single-family units rebounded 5.1 percent to an annual rate of 1.036 million units, after falling 4.2 percent in March and 14.2 percent in February.
- Following two consecutive months of substantial declines, sales of new single-family homes staged a comeback in April, leaping 10.9 percent to a seasonally adjusted annual rate of 620 thousand units. New home sales are expected to climb modestly during the second quarter, a trend which could be strengthened if interest rates continue to decline during June.
- Existing single-family home sales declined for the fourth consecutive month in April, sliding to an annual rate of 3.36 million units, or 1.2 percent slower than the March annual rate of 3.4 million units. However, with the recent retreat in interest rates, existing home sales are most likely at, or near, their low point for 1989.
- The median price of an existing single-family home rose 1.6 percent in April to $93,500, marking the fifth consecutive monthly advance. Meanwhile, the sales price of a new single-family home plunged 7.1 percent to $117,000.

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REALTOR®

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SOMETHIN'S HAPPENIN' HERE

Economic Commentary

by
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Mobs of students battle authority in the central park of a major city while important political meetings take place nearby; politicized rock bands blare their messages from underground locations to the consternation of the establishment. The U.S. in 1968. No. China and the U.S.S.R. in 1989? Yes. Sure is a different world out there. In the words of Steven Stills, "Somethin's happenin' here, and what it is ain't exactly clear...." Well, let's take a crack at an explanation.

Several years ago (before it became as usual as a bus trip across town), a friend visited Australia. When I asked him what it was like, he described it as the U.S. in the Fifties. And while history doesn't repeat itself in quite the same way every time, we may now be able to describe the Eastern Bloc as the U.S. in the Sixties. In both China and the Soviet Union, we are witnessing a ferment generated from a generation for whom the capitalist door has been held slightly ajar. And because both societies have become more capitalist, the level of tension between us and them has dropped noticeably (as the late Emily Litella would ask, "What's all this about glass noses?"). The world, in short, is converging at a bewildering rate, and because the Russians and the Chinese have seen a little market economics personally and because the media has shown them the rest, their youth has become as restless as the angry Boomers were in the Sixties right here.

We see the homogenization of the world economy in a variety of ways, but not always with the same eyes. The consumer who is tickled to see the pressure of Japanese, German, British and Korean imports touch off fire sales at dealers of American cars looks at life a bit differently from the auto worker whose job on the line is on the line. And beyond these tangible signs of our interdependency with other nations, there is a pervasive consciousness of, and growing sensitivity to, events and conditions throughout the global village. To a great degree, electronics have shrunk space. We transmit money and images instantaneously and o interest in Japanese politics and British stock prices goes up considerably.

But let's bring this a little closer to home. The real estate community has been increasingly concerned about the spread of foreign ownership of American property. In part, this is a function of our considerable foreign trade deficit -- after all, you can only spend dollars in the U.S. But it's also a function of the remarkably lower prices commercia! real estate fetches in the U.S. compared to similar buildings abroad. This has been true for quite some time, and some foreign investors have been here for a while. But the shrinking of the world and the tremendous interest in the workings of the American economy have let out the closely held secret, with the resulting boom in foreign ownership.

Secondly, the barrage of information that has resulted from fiber optics and miniaturization has jaded the American public, but has made that public a more knowledgeable consumer. The "secrets of the temple" that had made the financial sector so impenetrable have been exposed by an avalanche of financial news reporting. The result is that the home buyer knows more about interest rates and mortgage types than any of us would have thought possible as recently as ten years ago. Moreover, the video age has produced consumers who receive messages electronically, challenging real estate professionals to think long and hard about marketing techniques that can capitalize on the new sophistication. Clearly, this is a new, but continuing twist on the constant challenge of selling real estate.

Finally, the electronic convergence of the world has blurred the lines that previously separated aspects of the real estate transaction and will continue to do so. The current debate over computerized mortgage origination and the role of the real estate broker has its genesis in the capacity to telescope the mortgage lending process. In reality, the real estate office is just a way station in the evolution and may in fact be superceded by the direct contact via computer between the provider of funds and the user of funds. But, at the moment, the whole mortgage financing landscape is shifting and those involved are understandably confused at the change.

It's a human characteristic that we fail to notice the occurrence of events that later go on to have tremendous impact on everyday life. Recently, this came to mind with the passage of the 50th anniversary of the invention of the pay phone. In a sen, the things that will be the crucial influences on our lives are coming into being now. But unlike the past, when few knew when things happened, so much is occurring that mere knowledge is not the problem; rather, understanding and the time necessary to understand are what fail us.

Outlook for the Economy and Real Estate

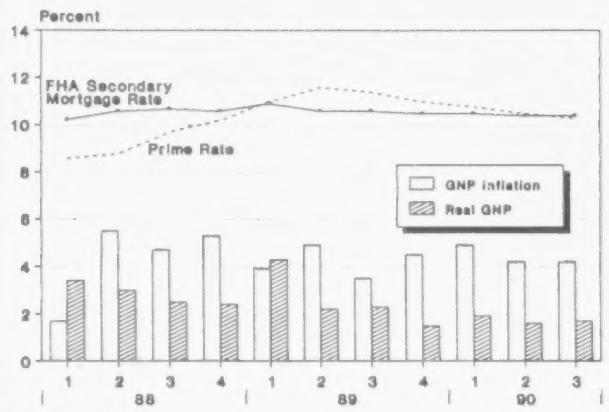
ECONOMIC OUTLOOK

The U.S. Department of Commerce cut its estimate of first quarter real GNP growth dramatically to 4.3 percent from 5.5 percent, indicating a much slower rate of economic activity in the opening months of 1989. The Commerce Department did not, however, modify its drought adjustments which added 2.5 percentage points to the first quarter growth estimate. The revision, then, was principally to real non-farm growth which slowed to an annual rate of 1.8 percent, well below the 3.5 percent non-farm growth rate in the fourth quarter of 1988. While the recent revision did allay fears that the economy may be overheating and thus heading for a difficult struggle with inflation, it also added fuel to growing concerns that the Federal Reserve may have tightened the money supply a bit too much, risking a future brush with a recession. However, the composition of the downward revision suggests otherwise. The revision was encouraged primarily by a 64 percent reduction in the estimate for inventory accumulation, from $24.7 billion to $8.9 billion. Large stock piles near the end of an expansion generally lead to recessionary fears, in that they tend to spur production cutbacks and employment layoffs. Such a large downward revision in the inventory number suggests this is not at hand. The net exports estimate was revised upward by 80 percent to $17.6 billion, while the consumption and fixed investment estimates were lowered slightly.

Just as increased inventory investment can enhance the risk of a recession, business fixed investment in structures and equipment can do the opposite. Fixed investment increases capacity and productivity, thereby reducing the chances of backlogs and shortages. Further, it boosts U.S. competitiveness vis-a-vis the rest of the world. A closely watched barometer of future business fixed investment is the rate of new orders for non-defense capital goods. This indicator has been sluggish during the first quarter of 1989, reflecting the rather strong fixed investment in equipment (up 8.3 percent in the first quarter after falling 3.3 percent in the fourth quarter of 1989) already underway at the nations factories. However, in April orders shot up by 6.1 percent in what amounted to the largest monthly advance since December of 1988. Further indications of the surprisingly good health at the nations factories came from a 2.7 percent jump in new orders for manufactured goods, following three months of declining or anemic growth.

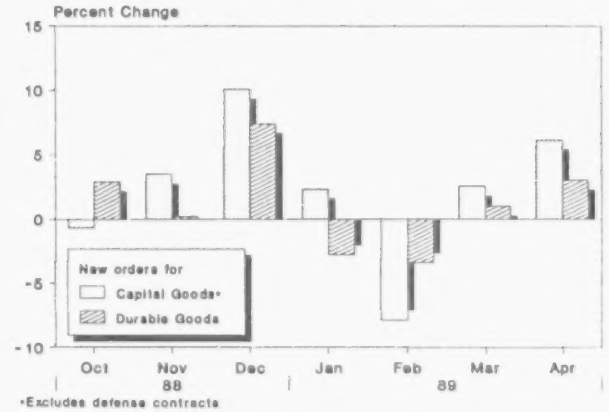
The 0.8 percent rise in the index of leading economic indicators in April offered additional proof of the economy's continued buoyancy. The index is designed to foreshadow economic growth by combining 11 separate economic indicators (unemployment claims, length of the average work week, consumer and capital goods orders, inventories, selected raw materials and stock prices, money supply, building permits, and delivery speed) generally thought to be good gauges of future economic activity. The April gain was widespread, with only consumer confidence, money supply, and materials prices pulling the index down, while all other eight components showed considerable signs of strength. The April rise broke a two month series of declines -- an important signal in itself -- as three consecutive monthly declines are sometimes thought to foreshadow an upcoming recession. Nevertheless, April's report helped calm the recessionary fears heightened by a flurry of negative economic reports for February and March.

GRAPH 1: THE ECONOMIC OUTLOOK



E NAR estimates

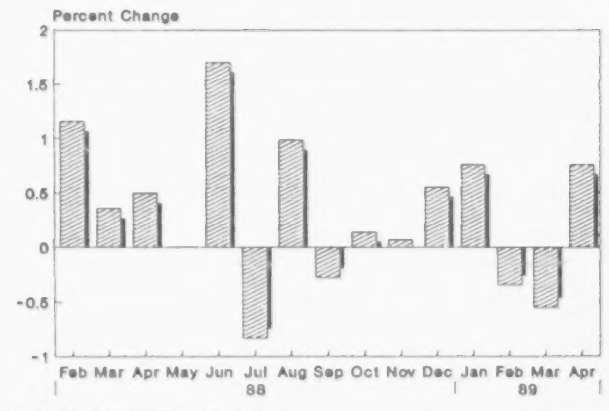
GRAPH 2: NEW ORDERS FOR MANUFACTURED GOODS MAKE A COMEBACK IN APRIL



*Excludes defense contracts

Source: Advance Report on Durable Goods Shipments and Orders.

GRAPH 3: THE INDEX OF LEADING INDICATORS SHOWS NEW ECONOMIC STRENGTH



Source: The Bureau of Economic Analysis.

The New Strength of the Dollar

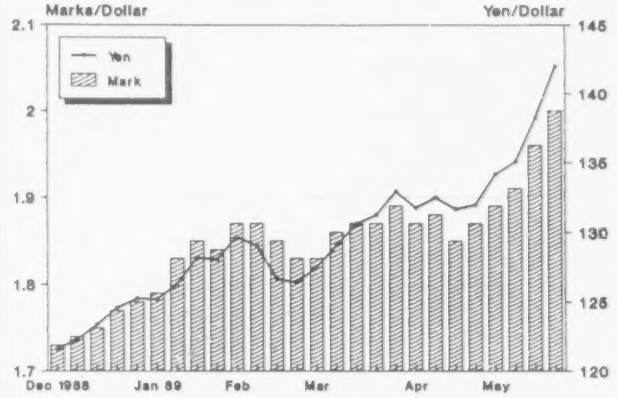
The dollar reached a 29 month high in May, encouraged primarily by high U.S. interest rates relative to those in Germany, Japan and the U.K. In addition, political problems in Europe and Japan, higher oil prices, and the attraction of the U.S. stock and bond markets to foreign investors, all added to the new found interest in the dollar. The result has been to take the dollar well out of the 1.7-1.9 mark and 120-140 yen trading ranges believed to be set by the G-7 ministers (economic ministers of the U.S., Great Britain, West Germany, France, the Netherlands, Canada, and Japan), and above what have become psychologically important barriers of 2.0 marks and 140 yen. The higher dollar will most likely complicate efforts by U.S. manufacturers to increase exports, as a rise in the dollar of this magnitude more than erases months of productivity gains. This would in turn slow the export driven growth that many policy makers are hoping will allow for the economic "soft landing" during the next year. In addition, a higher dollar may reverse the trend of improvement in the trade deficit which fell in March to $8.9 billion from $9.8 in February. In the opening days of June the dollar began to show some signs of retreat, following a round of concerted central bank intervention and the first increase in the Japanese discount rate in nine years, from 2.5 to 3.25 percent. However, an easing of U.S. interest rates in the coming weeks will likely be necessary to reduce the attraction of dollar-denominated investments in relation to comparable foreign securities.

MONETARY POLICY AND INTEREST RATES

The rising U.S. dollar, combined with signs of slower economic growth and moderate inflation (the CPI rose by a modest 0.2 percent excluding energy in April), has led the Federal Reserve to consider a policy of looser credit in recent weeks. Although the Fed did not join the Japanese central bank in a concerted interest rate change (a step which would have strengthened considerably the G-7's control over exchange rates) there is some indication that the Fed will ease its credit policy in the coming weeks. Most analysts are expecting a 0.25 percentage point drop in the federal funds rate, which has fluctuated in a narrow range of 9.75 to 9.85 for over two months. Interest rates have drifted lower over the past two months, primarily on the news of subdued economic growth and expectations of slower rates of inflation. Graph 5 shows how the initial drop in interest rates during April came at the short end of the yield curve, while more recent declines have been concentrated on long term rates. The result has been a near flattening of the yield curve with rates on all terms ending May more than 50 basis points below those prevailing in March.

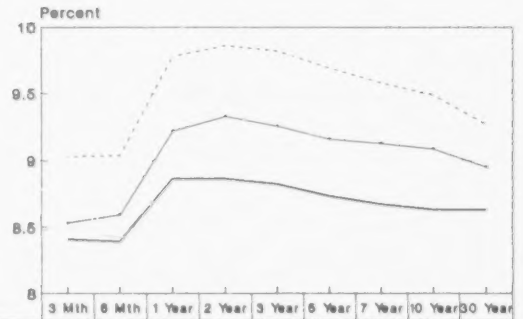
In response to the recent bond rally, fixed-rate mortgages have fallen to their lowest levels so far in 1989. The average rate on a conventional fixed-rate mortgage has plunged by almost 100 basis points in the past two months, to 10.5 percent in the final week of May. More aggressive lenders have been offering rates as low as 10.25 percent on a 30-year fixed rate mortgage. If the Federal Reserve loosens credit in the coming weeks as expected, mortgage rates will most likely fall even further, particularly those on ARMs whose recent decline has been less dramatic. Lower rates could draw homebuyers off the fence and into the market this summer, bolstering sales which have been weak so far this year.

GRAPH 4: THE DOLLAR RISES AGAINST THE MARK AND THE YEN



Source: Generale de Banque, New York.

GRAPH 5: THE YIELD CURVE



	3 Mth	6 Mth	1 Year	2 Year	3 Year	5 Year	7 Year	10 Year	30 Year
Mar 25 ----	9.03	9.04	9.78	9.86	9.82	9.69	9.58	9.49	9.27
Apr 25 ——	8.53	8.59	9.22	9.33	9.26	9.16	9.13	9.09	8.95
May 26 ——	8.41	8.39	8.86	8.86	8.82	8.73	8.67	8.63	8.63

Source: The Federal Reserve Board.

GRAPH 6: FIXED-RATE MORTGAGES FALL TO THEIR LOWEST LEVEL OF THE YEAR

*Contract interest rates on commitments for fixed-rate first mortgages.

Source: Board of Governors of the Federal Reserve System.

HOUSING STARTS

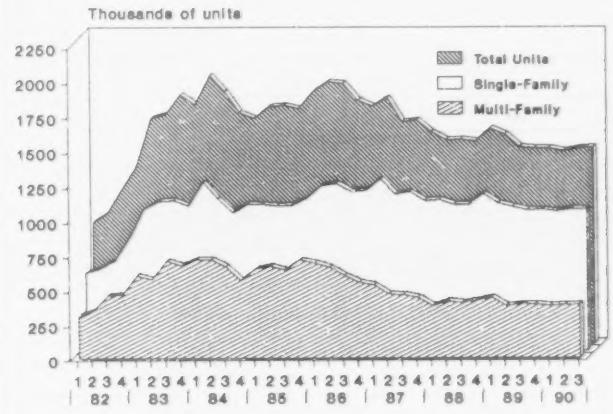
(Seasonally Adjusted Annual Rates, in Thousands)

		Total	S-F	2-4	5 and up
Apr	1989	1361	1036	68	257
Mar	1989	1399	986	51	362
Feb	1989	1465	1029	62	374
Jan	1989	1678	1199	66	413
Dec	1988	1577	1141	65	371
Apr	1988	11576	1087	58	431
April 1989 Change From:					
Mar	1989	-2.7%	5.1%	33.3%	-29.0%
Apr	1988	-13.6%	-4.7%	17.2%	-40.4%

		Northeast	Midwest	South	West
Apr	1989	208	227	529	347
Mar	1989	153	306	551	389
Feb	1989	224	273	572	396
Jan	1989	293	313	642	430
Dec	1988	210	343	609	424
Apr	1988	260	344	595	377
April 1989 Change From:					
Mar	1989	36.0%	-9.5%	-4.0%	-10.8%
Apr	1988	-20.0%	-19.5%	-11.1%	-8.0%

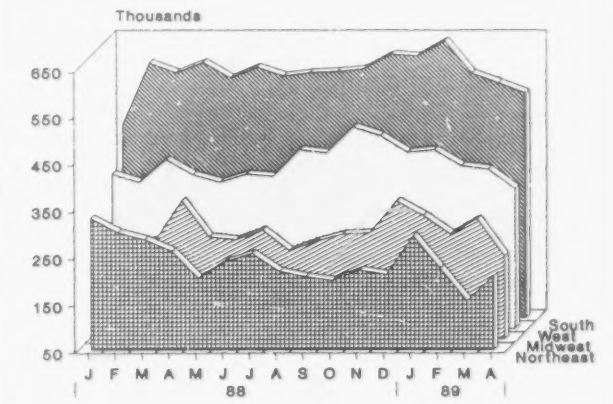
Source: Bureau of the Census; Construction Reports, Series C20

GRAPH 7: HOUSING STARTS



Source: The Bureau of Census; E NAR Estimates

GRAPH 8: HOUSING STARTS BY REGION



Source: The Bureau of Census

Prompted by a large drop in the construction of buildings with five or more housing units, housing starts slowed by 2.7 percent in April to an annual rate of 1.361 million units. However, starts of single-family units rebounded 5.1 percent to an annual rate of 1.036 million units, after falling 4.2 percent in March and 14.2 percent in February. In April, starts of multi-family units with five or more units fell 29 percent to an annual rate of 257 thousand units. Because of the large monthy swings in the starts of multi-family units, they tend to be a poor barometer of housing activity. The increase in single-family starts alleviated some fears that the housing industry may be heading for a recession. Furthermore, the decline in interest rates during May creates the possibility of even stronger rates of housing construction in the coming months. However, slower economic growth will continue to contain future housing construction, as housing starts will likely average between 1.4 and 1.43 million units through the rest of 1989.

Housing starts showed continued signs of weakness in every region except the Northeast, where starts were up 36.0 percent to an annual rate of 208 thousand units. However, this drop only partly compensated for the combined 47.8 percent drop during February and March. In the West, starts plunged 10.8 percent to a rate of 347 thousand units, slower than any rate since December 1987. Starts were down 9.5 percent in the Midwest and 4.0 percent in the South, at annual rates of 277 and 529 thousand units, respectively.

NEW HOME SALES

(Seasonally Adjusted Annual Rates, in Thousands)

NATIONAL DATA

Apr 1989	620	Sep 1988	691
Mar 1989	559	Aug 1988	555
Feb 1989	624	Jul 1988	691
Jan 1989	700	Jun 1988	712
Dec 1988	669	May 1988	701
Nov 1988	650	Apr 1988	716
Oct 1988	718		

Apr 1989
Changes From:

Mar 1989	10.9%	1987	671
Apr 1988	-8.4%	1988	677

REGIONAL DATA

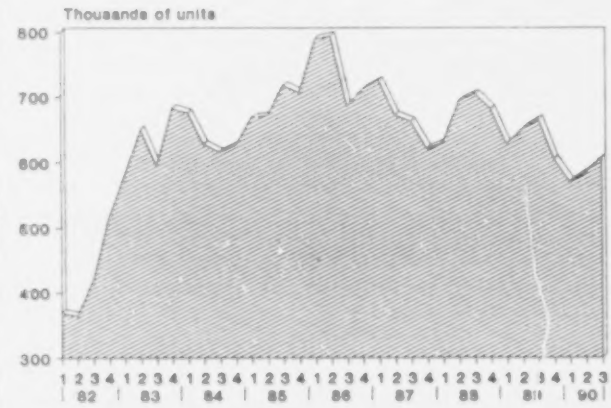
	Northeast	Midwest	South	West
Apr 1989	96	96	234	193
Mar 1989	116	103	193	147
Feb 1989	87	107	232	199
Jan 1989	121	106	265	207
Dec 1989	109	94	263	204
Nov 1988	65	104	254	227
Apr 1988	109	93	287	188
1988	102	97	275	202
1987	134	102	288	140

Apr 89
Changes From:

Mar 1989	-17.2%	-6.8%	21.2%	31.3%
Apr 1988	-11.9%	3.2%	-18.5%	2.7%

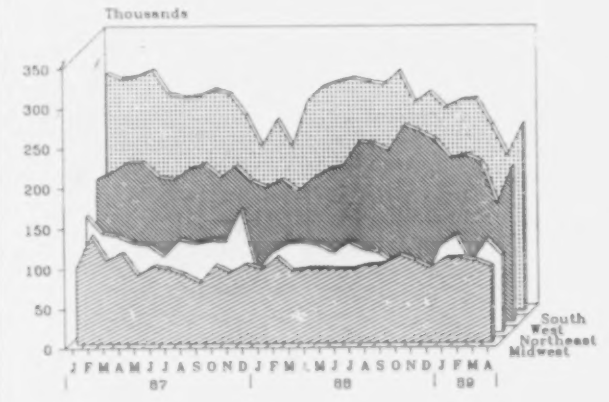
Source: Bureau of the Census, Construction Reports, Series C25

GRAPH 9: NEW HOME SALES



Source: The Bureau of Census; E NAR Estimates

GRAPH 10: NEW HOME SALES BY REGION



Source: The Bureau of Census

Following two consecutive months of substantial declines, sales of new single-family homes staged a comeback in April, leaping 10.9 percent to a seasonally adjusted annual rate of 620 thousand units. However, what amounted to the largest monthly increase since February 1988, only partly made up for the 20.1 percent decline from January to March: sales remained well below the 677 thousand unit rate of April 1988. New home sales are expected to climb modestly during the second quarter, a trend which could be strengthened if interest rates continue to decline during June. Sales will most likely remain stable in the third quarter before dropping off in the fourth with slower economic growth.

The April rebound was fueled entirely by a return to more "normal" rates of sales in the West and South, following depressed sales during February and March in both regions. In the West, sales climbed 31.3 percent to an annual rate of 193 thousand units. The impressive gain was not, however, strong enough to make up for the 3.9 and 26.1 percent declines during February and March, respectively. Sales were up 21.2 percent in the South at an annual rate of 234 thousand units. Here too, because of large declines during February and March, sales remained below the January rate of 265 thousand units. Sales continued their erratic, see-saw behavior in the Northeast, dropping 17.2 percent in April, following a 33.3 percent increase in March. In the Midwest, sales have maintained their relatively stable and steady course when compared to the other three regions, falling 6.8 percent to a seasonally adjusted annual rate of 96 thousand units.

EXISTING SINGLE-FAMILY HOME SALES

(Seasonally Adjusted Annual Rates, in Thousands)

NATIONAL DATA

Apr 1989	3360	Sep 1988	3640
Mar 1989	3400	Aug 1988	3690
Feb 1989	3480	Jul 1988	3650
Jan 1989	3550	Jun 1988	3800
Dec 1988	3920	May 1988	3620
Nov 1988	3710	Apr 1988	3510
Oct 1988	3680		

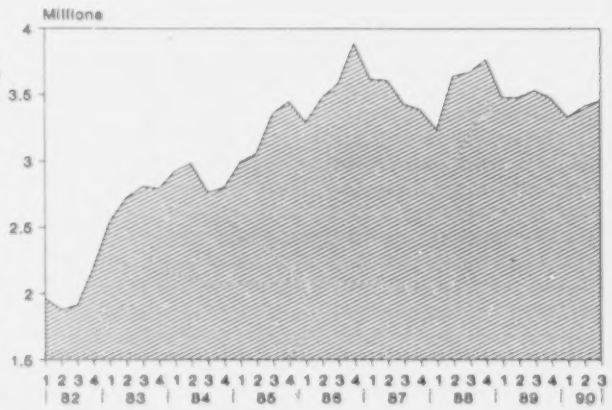
Apr 1989 Changes From:		Annual Totals:	
Mar 1989	-1.2%	1988	3594
Apr 1988	-4.3%	1987	3526

REGIONAL DATA

	Northeast	Midwest	South	West
Apr 1989	610	890	1270	620
Mar 1989	570	870	1270	670
Feb 1989	600	920	1310	640
Jan 1989	710	930	1310	630
Dec 1988	700	1010	1500	700
Nov 1988	680	940	1410	680
Oct 1988	640	940	1410	690
Apr 1988	600	910	1320	620
1988	673	929	1350	642
1987	685	959	1282	600
Apr 1989 Changes From:				
Mar 1989	7.0%	2.3%	0.0%	-7.5%
Apr 1988	-7.6%	-2.2%	-3.8%	0.0%

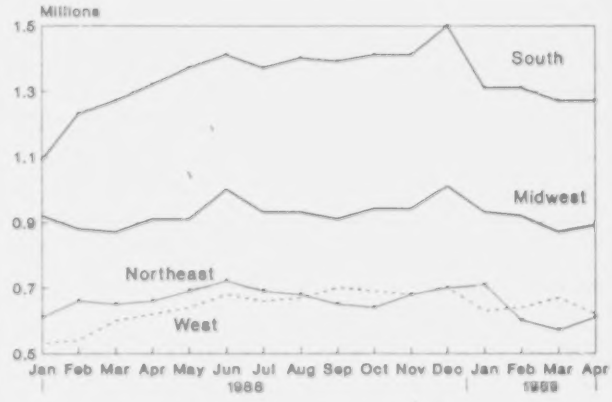
Source: NATIONAL ASSOCIATION OF REALTORS®, Economics and Research Division

GRAPH 11: EXISTING HOME SALES



Source: The Bureau of Census; E NAR Estimates

GRAPH 12: EXISTING HOME SALES BY REGION



Source: NAR Economics and Research; E NAR Estimates

Existing single-family home sales declined for a fourth consecutive month in April, sliding to an annual rate of 3.36 million units, or 1.2 percent slower than the March annual rate of 3.4 million units. The April existing home sales rate was down 4.3 percetn from the April 1988 annual rate of 3.51 million units. Overall, the pace of existing home sales through the first four months of 1989 is virtually identical to 1988 sales volume over the same period. The big difference is in the trend: home sales started slowly in January 1988 and increased through April and beyond; whereas, in 1989, home sales showed considerable strength in January, but have slowed steadily ever since. However, with the recent retreat in interest rates, existing home sales are most likely at, or near, their low point for 1989.

Regionally, existing home sales moved in precisely the opposite direction as sales of new homes, with sales of existing homes picking up speed in the Northeast and Midwest, while sales in the West and South were sluggish. In the Northeast, sales of existing homes jumped 7.0 percent to an annual rate of 610 thousand units. After falling for three consecutive months, sales in the Midwest rose moderately by 2.3 percent to an annual rate of 890 thousand units. In the South, sales remained unchanged at an annual rate of 1.27 million units. The West was the only region to experience a decline in April, where sales dropped 7.5 percent to an annual rate of 620 thousand units, even with the sales rate of a year ago, and slower than any rate since then.

SINGLE-FAMILY HOME PRICES

	Median		Average	
	Existing	New	Existing	New
Apr 1989	$93,500	117,000$	$118,200	145,700$
Mar 1989	92,000	126,000	116,100	150,500
Feb 1989	91,900	119,000	117,800	147,000
Jan 1989	89,700	113,000	113,000	138,600
Dec 1988	88,700	121,000	112,000	147,700
Apr 1988	$88,000	111,000$	$109,600	135,600$
1988	89,300	112,500	112,800	138,200
1987	85,600	104,500	106,300	127,200
Apr 1989 Changes From:				
Mar 1989	1.6%	-7.1%	1.8%	-3.2%
Apr 1988	6.4%	5.4%	7.8%	6.7%

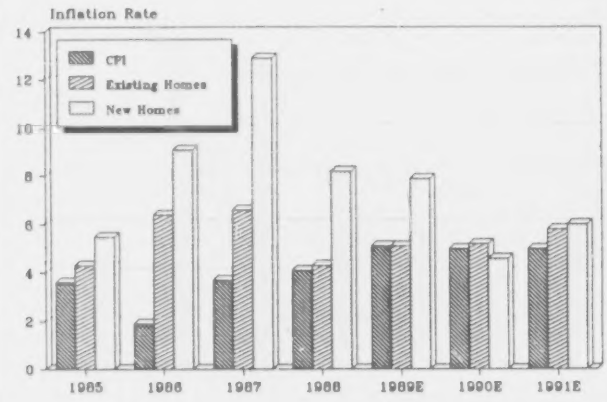
REGIONAL DATA

MEDIAN SALES PRICE OF AN EXISTING HOME

	Northeast	Midwest	South	West
Apr 1989	$144,300	$70,500	$86,100	$140,700
Mar 1989	143,600	69,900	84,000	138,000
Feb 1989	142,600	69,900	86,700	127,800
Jan 1989	143,800	67,800	82,400	130,700
Dec 1988	143,000	67,700	78,200	128,700
Apr 1988	$141,000	$67,600	$81,000	$117,700
1988	143,000	68,400	82,200	124,900
1989	133,300	66,000	80,400	113,200
Apr 1989 Change From:				
Mar 1989	0.5%	0.9%	2.5%	2.0%
Apr 1988	2.3%	4.3%	6.3%	19.5%

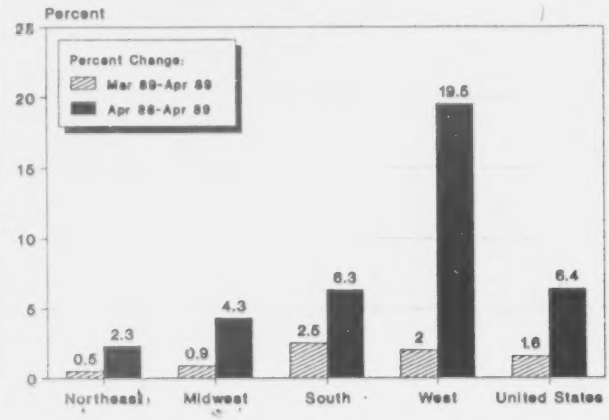
Source: NATIONAL ASSOCIATION OF REALTORS®, Economics and Research Division

GRAPH 13: HOME PRICES



Source: The Bureau of Census; E NAR Estimates

GRAPH 14: HOME PRICES BY REGION



Source: NAR Economics and Research; E NAR Estimates

The median price of an existing single-family home rose 1.6 percent in April to $93,500, marking the fifth consecutive monthly advance. Meanwhile, the sales price of a new single-family home plunged 7.1 percent to $117,000. Much of the April movement in home prices can be traced to regional shifts in sales. While sales of new homes increased, sales declined in the Northeast, the highest priced region in the country, and rose dramatically in the South, where the median home price is less than the national median. Exactly the opposite was true for sales of existing homes, with sales rising 7.0 percent in the Northeast and remaining unchanged in the South.

While the Northeast continues to retain its position as the highest priced region of the country, the West may take over this title before the end of this year. In the year ending April 1989, the median price of an existing single-family home rose 19.5 percent to $140,700, while home prices in the Northeast increased by only 2.3 percent to $144,300. Home prices in the South have been showing renewed strength in recent months, rising 2.5 percent in April to $86,100. In the Midwest, prices continue to show moderate, steady growth rising 0.9 percent in April, and 4.3 percent for the year, to $70,500.

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PROSPECTIVE FIRST-TIME HOMEBUYERS: THEIR CHANGING FINANCIAL POSITIONS

House prices, household incomes, household savings and wealth, monthly housing expenses, mortgage interest rates, mortgage instruments, and loan underwriting criteria -- each is a dimension of housing affordability, most of whose trends are discussed in the November 1988 *Outlook for the Economy and Real Estate* article, "Explaining Trends in Homeownership."[1] Each of these dimensions can be placed into two broad aspects of the affordability of homeownership -- the ability of a household to make the transition to homeownership and the ability of a household to meet the ongoing expenses of homeownership. Here, as in the April *Outlook* article, "The Assets of Prospective First-time Homebuyers: A Look at the 1983 and 1986 Surveys of Consumer Finances," we will address the former -- the ability of a renting household to make the transition to homeownership.

In April's issue, we looked at the characteristics which truly make a "potential" first-time homebuyer "prospective." Simply put, our "potential" first-time homebuyer is a household which has never owned a home (based on assumptions laid out in the previous article.) Moreover, the median age of the first-time homebuyer remains between 25 and 34 years, and accordingly we limited our potential first-time homebuyers to renting households within this age group. We further limited our potential first-time homebuyers to those with incomes sufficient to meet the ongoing expenses of homeownership. Because we found a disproportionately large share of renting households relative to homeowners (ages 25 through 34) with low incomes, we further constrained our sample to renting households with 1985 incomes of $20,000 or more. This is our target group, referred to as "prospective first-time homebuyers."

Throughout the April article, the financial and real assets of the samples of "prospective first-time homebuyers" were compared to those of "first-time homeowners" and "non first-time homeowners," similarly constrained by age and income. A sample of "non first-time homeowners," unconstrained by age and income, was included in the tables but was not discussed. This article will be structured in a similar manner. However, in contrast to the previous article in which we looked at the median values for those households holding each asset type, we will look primarily to average values for all households. Moreover, unlike the last article the data will be weighted by Federal Reserve computed weights.[2]

The Assets and Liabilities of Prospective First-time Homebuyers

The ability to meet the ongoing expenses of homeownership is best explained by the current income, education and vocational training, profession, etc. (as proxies for "lifetime earnings") of a household. However, the ability to make the transition to homeownership is best explained by the stock concepts of household wealth and savings.

In "The Assets of Prospective First-time Homebuyers," we saw that only small percentages (less than one-third in many cases) of young households -- prospective first-time homebuyers, first-time homeowners and non first-time homeowners alike -- held assets other than checking and savings accounts and vehicles. Table 1 shows both the average 1986 dollar holdings and the percentage of households holding each asset type.[3] For 7 asset types, prospective first-time homebuyers have lower average 1986 values than both first-time and non first-time homeowners of similar age and income. These include bonds, IRA and Keogh accounts, money market accounts/CDs, cash value of life insurance, "other" financial assets, non primary residence real estate and vehicles. Additionally, the average value of liquid assets, or those most easily converted to a home equity downpayment, of prospective first-time homebuyers is only 78% and 71% of the liquid assets of first-time and non first-time homeowners, respectively.

On the other hand, the average values of stocks and mutual funds, checking and savings accounts, profit sharing and thrifts and business assets of prospective first-time homebuyers are greater than those of first-time homeowners but less than those of non first-time homeowners. This shortfall of first-time homeowners may reflect the liquidation of some assets by the first-time homeowners for the home purchase, while the non first-time homeowners have had time to replenish the savings they may have used for a home downpayment. On average, total assets (excluding the current value of primary residences of homeowners) of prospective first-time homebuyers was below that of both groups of comparable homeowners -- $31,752 vs. $40,560 and $44,475. When the current value of the primary residences of the homeowners is included, the gap widens substantially -- $31,752 vs. $121,181 and $114,670, respectively.

Liabilities are also an important component of the affordability of homeownership. Even if a prospective first-time homebuyer believes that he/she can take on the burden of a mortgage, the lender may feel otherwise, particularly in light of recent high rates of delinquency and foreclosure. The debt outstanding of prospective first-time homebuyers appears to be, on average, lower than that of the comparable homeowners. (See Table 2.) In fact, the average 1986 debt (excluding mortgage debt on primary residences for homeowners) of non first-time homeowners was 43% higher and that of first-time homeowners was

TABLE 1

1986 Financial and Real Assets
Average 1986 dollar values (and percent of households holding)* for:

	Prospective First-Time Homebuyers	First-Time Homeowners	Non First-Time Homeowners	Non-First Time Homeowners (all ages & income)
FINANCIAL				
Stocks and Mutual Funds	$790(27.4%)	$756(25.3%)	$904(18.9%)	$21,695(23.7%)
Bonds	208(14.5)	1,256(27.0)	1,268(29.7)	8,457(25.7)
Checking and Savings Acct	3,668(100.0)	3,157(98.9)	4,133(98.2)	8,054(95.2)
IRA and Keogh Accts.	1,126(20.0)	1,427(35.5)	1,300(30.0)	7,745(34.3)
Money Market & CD's	1,678(21.9)	3,014(25.7)	2,683(24.5)	12,435(35.2)
Profit Sharing and Thrift Accounts	1,237(27.9)	1,180(26.1)	2,240(25.8)	5,855(16.6)
Life Insurance, cash value	987(20.1)	1,563(31.4)	4,881(34.7)	5,157(43.4)
Other Financial Assets	9(0.4)	278(2.2)	330(3.7)	8,637(6.8)
Liquid Assets**	6,345	8,183	8,988	50,641+
REAL				
Real Estate, other than primary residence	9,813(15.1)	10,670(15.1)	10,299(18.9)	38,081(28.2)
Business Assets	5,361(4.5)	4,990(12.6)	7,915(19.2)	39,685(16.4)
Vehicles	6,875(93.0)	12,269(99.0)	8,523(100.0)	8,238(92.0)
TOTALS				
Total Financial Assets***	9,703	12,631	17,739	78,035
Total Real Assets****	22,049	27,929	26,736	86,004
Total Assets*****	31,752	40,560	44,475	164,039
Current Value of Primary Residence	0	80,621	70,195	81,770
Total Assets******	31,752	121,181	114,670	245,809

*All values are weighted by Federal Reserve Board computed weights.

**Liquid assets is the average over all households of the sum of stocks and mutual funds, bonds, checking and savings accounts and money market accounts and CDs for each household.

***Total financial assets is the average over all households of the sum of the 8 financial assets in the Table, except liquid assets which is composite of several assets, for each household.

****Total real assets is the average over all households of the sum of the 3 real assets in the Table for each household. Please note this excludes the current value of primary residences for homeowners.

*****This is the average value over all households of the sum of the 8 financial and 3 real assets of the Table for each household. Please note this excludes the current value of primary residences for homeowners.

******This is the average value over all households of the sum of the 8 financial and 3 real assets and current market value of primary residences for each household. The inclusion of the current value of primary residences substantially increases the total assets of homeowners.

SOURCE: NATIONAL ASSOCIATION OF REALTORS® tabulations of 1986 Survey of Consumer Finances, Federal Reserve Board.

TABLE 2

1986 Debt Outstanding

Average 1986 dollar values*
(and percent of households having) for

	Prospective First-time Homebuyers	First-time Homeowners	Non First-time Homeowners	Non First-time Homeowners (all ages & incomes)
Mortgage Debt, properties other than primary residence	$871 (2.9%)	$5,043 (12.4%)	$3,036 (6.8%)	$9,358 (11.5%)
Installment Debt, loans for additions and repairs to home	0 (0.0)	378 (8.0)	455 (9.4)	375 (6.6)
Installment Debt, automobile, truck and vehicle loans	1,905 (37.8)	4,875 (45.3)	2,066 (41.0)	1,495 (24.8)
Installment Debt, furniture, appliance, recreation, or hobby loans	33 (5.3)	231 (13.9)	134 (11.3)	106 (6.9)
Installment Debt, "other" loans with regular payments	1,668 (20.0)	512 (23.0)	871 (16.9)	472 (11.7)
Nonregular Payment Consumer Installment Debt	391 (13.2)	288 (7.6)	250 (6.2)	766 (7.2)
Credit Card Debt	530 (46.9)	1502 (62.0)	912 (63.6)	689 (46.6)
Total Debt**	5,398	12,829	7,725	13,261
Mortgage Debt (first and second mortgages) on Primary Residence	0(0.0)	54,051 (91.7)	35,170 (93.2)	18,339 (55.9)
Total Debt***	5,398	66,880	42,895	31,600

* All values are weighted by Federal Reserve Board computed weights.

** This total debt does not include the debt outstanding (first and second mortgages) on primary residences, whose inclusion substantially increases the total dollar value of debt outstanding for the homeowners. Total debt is the average over all households of the sum of the 4 debt types of the Table for each household.

*** This includes the debt outstanding (first and second mortgages) on primary residences for homeowners. Total debt is the average over all households of the sum of the 8 debt types of the Table for each household.

SOURCE: NATIONAL ASSOCIATION OF REALTORS®, tabulations of the 1986 Survey of Consumer Finances, Federal Reserve Board.

TABLE 3

1986 Balance Sheets

Average 1986 values* for:

	Prospective First-Time Homebuyers	First-Time Homeowners	Non First-Time Homeowners	Non First-Time Homeowners (All ages & incomes)
EXCLUDING CURRENT VALUE OF PRIMARY RESIDENCE AND DEBT THEREUPON				
Total Assets	$31,752	$40,560	$44,475	$164,039
Total Debt	$5,398	$12,829	$7,725	$13,261
Net Worth	$26,354	$27,731	$36,750	$150,778
INCLUDING CURRENT VALUE OF PRIMARY RESIDENCE AND DEBT THEREUPON				
Total Assets	$31,752	$121,181	$114,670	$245,809
Total Debt	$5,398	$66,880	$42,895	$31,600
Net Worth	$26,354	$54,301	$71,775	$214,209

* All values are weighted by Federal Reserve Board computed weights.

SOURCE: NATIONAL ASSOCIATION OF REALTORS® tabulations of the 1986 Survey of Consumer Finances, Federal Reserve Board.

two and one third times higher than the 1986 debt of prospective first-time homebuyers -- $7,725 and $12,829 vs. $5,398. Prospective first-time homebuyers, on average, had less mortgage debt on real estate other than primary residences, less credit card debt and less regular payment consumer installment debt on automobile, truck and vehicle loans, furniture, appliance, recreation and hobby loans. In contrast, prospective first-time homebuyers had, on average, over three and two times the amount of "other" regular payment installment debt, such as loans for education and medical expenses, than first-time and non first-time homeowners, respectively.

Table 3 summarizes the 1986 wealth of prospective first-time homebuyers vis-a-vis the other household types. When the current value of the primary residences of the homeowners and debt thereupon is not considered, the difference in the net worth of prospective first-time homebuyers and first-time homeowners is small, $26,354 vs. $27,731. However, when the current value of the primary residences of homeowners net of the mortgage debt is considered, the difference in the net worth of prospective first-time homebuyers and first-time homeowners widens substantially -- $26,354 vs. $54,301.

How Do They Save?

A sample of first-time homebuyers from the National Association of REALTORs' 1986 Homeownership Survey indicated that on average, the largest share (64%) of the home downpayment came from personal savings. Table 4 gives us an idea of how the 32.0% of prospective first-time homebuyers indicating that their primary reason for saving was to buy their own homes (from the 1986 Survey of Consumer Finances) actually saved. First, prospective first-time homebuyers saved more in financial assets between 1983 and 1986, $9,141 compared to $6,431 for first-time homeowners and $5,998 for the non first-time homeowners. Moreover, those prospective first-time homebuyers saving for a home appeared interested in the liquidity of their financial assets. While the average change from 1983 to 1986 in liquid assets of the young renting households saving for their first homes was $5,390 ($3,825 of which represented growth in checking and savings -- the most liquid asset type), the growth in liquid assets was only $3,819 for first-time homeowners and $3,216 for comparable non first-time homeowners. One could conjecture that the young first-time homeowners were in a "rebuilding period," much of their liquid savings having gone toward home downpayments and closing costs.

Prospective first-time homebuyers also appeared to be cautious about incurring debt while saving for homes. (See Table 4.) On average, their consumer installment debt increased by only $44 over the 1983 to 1986 period; whereas, first-time homeowners' installment debt rose by $3,553. On average, non first-time homeowners actually reduced their consumer installment debt by $495 over the 3-year period. Similarly, while the average credit card balances of young first-time and non first-time homeowners increased by $1,191 and $470 from 1983 to 1986, prospective first-time homebuyers' credit card balances increased by just over $300. The large increase in the credit card balances of first-time homeowners may reflect the "payment shock" often experienced by new homeowners.

Conclusion

The evidence suggests that many renting households strongly desire homeownership, with nearly one-third of prospective first-time homebuyers from the 1986 Survey of Consumer Finances indicating this as their primary reason for saving. Many seem to be trying to better position themselves financially for the transition, as evidenced by increasing asset balances, particularly liquid asset balances, and declining loan and credit card balances. In some housing markets, these measures will probably make homeownership a reality for many renting households with sufficient resources to meet the ongoing expenses of homeownership; but in many other markets, such measures will be insufficient and homeownership will be denied, or at least deferred, for many households.

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1.Excellent sources on homeownership affordability include David A. Crowe and Douglas B. Diamond, Jr., "Trends in Homeownership: 1980 to 1985," paper prepared for AREUEA/AEA meeting, Dec. 1985 and William C. Apgar, Jr. and H. James Brown "State of the Nation's Housing: 1988," prepared for the Joint Center for Housing Studies of Harvard University.

2.For a complete discussion of the development of the 1986 sample weights, see Robert B. Avery and Arthur B. Kennickell, Board of Governors of the Federal Reserve System, 1986 Survey of Consumer Finances: Technical Manual and Codebook.

3.The percentage of households holding each asset type reported here may differ from that reported in Table 2 of the April Outlook for the Economy and Real Estate article, "The Assets of Prospective First-time Homebuyers: A Look at the 1983 and 1986 Surveys of Consumer Finances." The reason for the divergence is that while we compared the percentages of unweighted samples in that article, the samples are weighted here to reflect the true 1986 population.

TABLE 4

Households' Changing Financial Positions

	Prospective First-time Homebuyers*	First-time Homeowners	Non First-time Homeowners	Non First-time Homeowners (all ages-incomes)
Average Changes in values from 1983 to 1986 in the following:				
FINANCIAL ASSETS				
Stocks and Mutual Funds	$290	$229	$456	$4,694
Bonds	3	388	144	2,387
Checking and Savings Accts.	3,825	1,452	1,853	3,251
Money Market and CDs	1,272	1,750	763	2,379
Total Liquid Assets	5,390	3,819	3,216	12,711
IRAs and Keogh Accts.	1,201	1,326	863	4,977
Profit Sharing and Thrifts	2,183	1,084	1,629	3,058
Life Insurance, Cash Value	427	319	538	441
Other Financial Assets	(60)	(117)	(248)	2,415
Total Nonliquid Assets	3,751	2,612	2,782	10,891
TOTAL FINANCIAL ASSETS	9,141	6,431	5,998	23,602
REAL ASSETS				
Home	0	80,621	19,254	13,269
Other Real Estate	12,323	5,145	4,606	11,775
Business Assets	$18,134	$2,579	$2,482	$174
Vehicles	2,201	8,031	2,765	2,604
TOTAL REAL ASSETS	32,659	96,376	29,107	27,822
TOTAL ASSETS	41,800	102,807	35,105	51,424
REAL ESTATE DEBT				
Home Mortgages, First & Second	0	54,051	10,243	2,702
Mortgages on other real property first and second mortgages	(729)	2,795	1,482	4,128
TOTAL REAL ESTATE DEBT	(729)	56,846	11,725	6,830
CONSUMER INSTALLMENT DEBT				
Regular payment debt	1,439	3,829	186	292
Nonregular payment debt	(1,395)	(276)	(681)	(1,031)
TOTAL CONSUMER INSTALLMENT DEBT	44	3,553	(495)	(739)
CREDIT CARD DEBT	307	1,191	470	278
TOTAL DEBT	(378)	61, 590	11,700	6,369
NET WORTH	42,178	41,217	23,405	45,055

* This category only includes "prospective first-time homebuyers" as previously defined who expressed that their primary reason for saving is to buy a house.

SOURCE: NATIONAL ASSOCIATION OF REALTORS® tabulations of 1986 Survey of Consumer Finances, Federal Reserve Board.

U.S. ECONOMIC OUTLOOK

JUNE 1989

	QUARTERS								YEARS				
	ACTUAL		FORECAST						ACTUAL		FORECAST		
	88.4	89.1	89.2	89.3	89.4	90.1	90.2	90.3	1987	1988	1989	1990	1991
AGGREGATE ECONOMY													
Gross National Product (billions of dollars)	5000	5105	5193	5268	5346	5437	5515	5595	4527	4864	5228	5556	5907
% Change	7.6	8.7	7.1	5.9	6.1	7.0	5.9	6.0	6.8	7.5	7.5	6.3	6.3
% Change (w/out inflation)	2.4	4.3	2.2	2.3	1.5	1.9	1.6	1.7	3.4	3.9	2.8	1.8	1.9
Consumer Price Inflation (CPI)	4.4	5.4	6.2	3.9	5.1	5.1	4.9	4.9	3.7	4.1	5.1	5.0	5.0
GNP Inflation (GNP Deflator)	5.3	3.9	4.9	3.5	4.5	4.9	4.2	4.2	3.3	3.4	4.5	4.4	4.4
Unemployment Rate - Civilian	5.3	5.2	5.3	5.2	5.2	5.3	5.3	5.4	6.2	5.5	5.2	5.4	5.5
Civilian Employment-Household Basis (millions)	115.8	116.9	117.4	117.8	118.3	118.6	118.8	119.1	112.4	115.0	117.6	119.0	120.3
Percent change	2.2	3.7	1.6	1.6	1.5	1.0	1.0	0.9	2.6	2.3	2.3	1.2	1.1
Index of Industrial Production	139.9	140.6	141.4	142.7	143.4	144.2	144.8	145.4	129.8	137.2	142.0	145.0	147.4
Manufacturing Capacity Utilization	84.4	84.3	83.7	84.0	83.9	83.7	83.5	83.3	81.0	83.6	84.0	83.4	82.5
Domestic Auto Sales	7.5	6.9	7.3	7.0	7.1	7.1	7.1	7.1	7.1	7.5	7.1	7.1	7.0
Federal Tax Receipts (NIPA) as % of GNP	19.8	20.5	21.1	21.4	21.8	22.5	22.8	23.2	18.3	19.5	21.2	23.0	24.6
Federal Expenditures (NIPA) as % of GNP	23.0	23.7	23.7	24.0	24.3	24.8	25.1	25.4	21.5	22.4	23.9	25.3	26.7
Deficit(NIPA)	-157.5	-158.5	-130.8	-130.1	-125.9	-114.8	-112.3	-109.8	-157.8	-142.4	-136.3	-111.2	-105.7
as % of GNP	-3.2	-3.1	-2.5	-2.5	-2.4	-2.1	-2.0	-2.0	-3.5	-2.9	-2.6	-2.0	-1.8
REAL ESTATE MARKETS													
HOME SALES													
Total Single-family Home Sales (thousands, single-family resales plus 97 percent of single-family starts)	4877	4516	4494	4527	4469	4318	4414	4453	4648	4651	4501	4400	4459
Percent change – year ago	9.7	-2.0	-3.8	-3.5	-8.4	-4.4	-1.8	-1.6	-1.4	0.1	-3.2	-2.2	1.3
Existing Single-family Home Sales (thousands)	3773	3477	3480	3535	3475	3335	3415	3455	3526	3594	3492	3405	3455
Percent change – year ago	11.3	5.4	-4.5	-3.5	-7.9	-4.1	-1.9	-2.3	-1.1	1.9	-2.8	-2.5	1.5
Housing Starts (thousands)	1559	1514	1425	1418	1417	1397	1419	1421	1634	1496	1443	1416	1419
Percent change – year ago	1.7	2.5	-3.7	-3.3	-9.1	-7.7	-0.4	0.2	-9.8	-8.5	-3.5	-1.9	0.2
Single-Family Units	1138	1071	1045	1022	1025	1013	1030	1029	1157	1089	1041	1026	1035
Percent change – year ago	4.5	-2.3	-1.6	-3.6	-10.0	-5.4	-1.4	0.6	-2.2	-5.8	-4.5	-1.4	0.9
Multi-Family Units	420	443	380	395	392	384	389	392	477	406	403	390	384
2-4 Family Units	65	60	51	53	53	52	52	53	66	59	54	53	52
Percent change – year ago	16.0	5.9	-10.7	-6.5	-19.1	-13.3	2.4	-0.9	-22.6	-10.3	-8.0	-3.2	-1.5
5+ Family Units	355	383	329	342	339	332	336	339	412	347	348	337	332
Percent change – year ago	-8.2	18.3	-9.0	-2.0	-4.4	-13.3	2.4	-0.9	-24.4	-15.7	0.3	-3.2	-1.5
New Single-family Home Sales (thousands)	679	628	651	667	605	570	585	607	671	677	638	587	644
Percent change – year ago	9.3	-0.3	-6.6	-5.1	-10.9	-9.2	-10.1	-9.0	-10.5	0.9	-5.8	-8.0	9.7
Mobile Homes Shipped (thousands)	223	217	218	204	207	205	209	212	233	217	212	211	233
HOME PRICES													
Existing Home Prices - Median $(1000)	88.7	91.2	94.0	94.7	95.6	96.6	98.0	99.3	85.6	89.3	93.9	98.8	104.5
Percent change – year ago	4.4	3.9	5.7	5.0	7.8	5.9	4.3	4.9	6.6	4.3	5.1	5.2	5.8
New Home Prices - Median $(1000)	114.9	119.3	119.8	121.0	125.4	127.5	125.1	126.2	104.0	112.5	121.4	126.9	134.5
Percent change – year ago	2.8	5.7	6.1	5.3	9.1	6.9	4.4	4.3	13.0	8.2	7.9	4.6	6.0
FINANCIAL MARKETS													
Long-Term Interest Rates													
30-year FRM (FHA Secondary)	10.6	10.9	10.6	10.6	10.5	10.5	10.4	10.4	10.2	10.5	10.7	10.4	10.3
1-year ARM (without buydown)	8.5	8.8	9.0	8.7	8.5	8.5	8.5	8.4	8.5	8.5	8.8	8.5	8.6
Corporate AAA Bond Rate	9.5	9.7	9.5	9.4	9.3	9.3	9.2	9.2	9.4	9.7	9.5	9.2	9.3
Government Bond Rate	9.0	9.0	8.8	8.6	8.5	8.4	8.4	8.4	8.6	9.0	8.8	8.4	8.5
Short-Term Interest Rates													
Federal Funds Rate	8.5	9.4	9.9	9.7	9.4	9.0	8.7	8.5	6.7	7.6	9.6	8.7	8.9
3-month T-Bill Rate	7.7	8.5	8.6	8.4	8.1	7.9	7.6	7.5	5.8	6.7	8.4	7.6	7.8
Prime Rate	10.2	11.0	11.6	11.4	11.0	10.8	10.5	10.3	8.2	9.3	11.3	10.4	10.7
Discount Rate	6.5	6.7	7.0	7.1	7.1	6.9	6.7	6.5	5.7	6.2	7.0	6.6	6.5
Value of the U.S. Dollar (Trade-Weighted Avg.)	93.0	96.0	100.6	102.1	98.5	95.3	93.3	91.9	96.9	92.8	99.3	92.7	86.8
Percent change	-17.6	13.5	20.8	5.9	-13.1	-12.6	-8.0	-6.0	-13.6	-4.3	7.0	-6.6	-6.3

Source: Forecast produced using Laurence H. Meyer and Associates' model of the U.S. economy.
Assumptions and simulations by Dr. John Tuccillo, Dr Frederick Flick, Sean Burns and Beth Maerz.

EQUAL HOUSING OPPORTUNITY